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June 6, 2008

To: Supervisor Yvonne B. Burke, Chair
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Supervisor Michael D. Antonovich

From: William T Fujioka
Chief Executive Officer

Wendy L. Watanabe
Acting Auditor-Controller

MAY 2008 STATE CONTROLLER'S REPORT – DISTRIBUTION AND REPORTING OF LOCAL PROPERTY TAX REVENUE, PHASE TWO

On May 6, 2008, the State Controller's Office (SCO) issued its final, Phase Two Report regarding the practices of school districts, community colleges, and redevelopment agencies (RDAs) related to the distribution and reporting local incremental property tax pass-through revenues.

The review, mandated by the 2007-08 State Budget Act, reflects concern over the apparent discrepancy between property tax growth reported to the State Board of Equalization and the lesser amounts reported by K-12 school districts and community colleges. RDAs must share some revenues from post-1993 projects with, among others, local schools. The State Budget Act directed the SCO review because the State's backfill obligation to local schools had not diminished as much as anticipated given the robust growth of property taxes prior to 2007.

The SCO's review disclosed that a number of RDAs in Los Angeles County, and other California counties, have failed to make AB 1290 pass-through payments to affected taxing entities. For Fiscal Years 2005-06 and 2006-07, RDAs throughout Los Angeles County reportedly underpaid the K-12 schools and community colleges \$19.1 million and \$21.1 million respectively in AB 1290 pass-through payments, resulting in

approximately \$8.4 million and \$9.2 million in excess state general fund obligation to the schools. Over the same period of time, local schools failed to correctly report about \$42 million of pass-through revenues that the State should have been credited with. The State will seek to recover these overpayments. We foresee no fiscal impact on the County.

The SCO's report listed Los Angeles County's redevelopment agency, the Community Development Commission (CDC), among RDAs that failed to make AB 1290 pass-through payments to affected taxing entities. The CDC's exposure is modest compared to many other RDAs, in part because of the small scope of its projects and payments until recently. The Auditor-Controller will work with the CDC to rectify its pass-through obligations to taxing agencies. We have been in contact with representatives of CDC and will work to assist them in calculating their necessary AB 1290 pass-through payments.

Finally, the SCO's report implicitly criticizes the Auditor-Controller for withholding the County's General Fund share of AB 1290 pass-through payments before distributing the remaining portion to the RDAs. Currently, there is no law that requires the Auditor-Controller to make AB 1290 payments to taxing jurisdictions or to withhold the County's share. However, in 1994, the Auditor-Controller made a policy decision to withhold County General Fund share when AB 1290 became law and the RDAs acquiesced in this practice. Some RDAs, however, reported to SCO that they believed that the County had been making all AB 1290 pass-through payments to affected taxing entities on their behalf. The SCO noted that this erroneous belief did not relieve RDAs from their statutory responsibilities.

Senator Negrete McLeod, Chair of the Senate Local Government Committee, immediately introduced SB 360 to remedy the issues cited in the SCO's report in the future. Specifically, SB 360 would impose on the Auditor-Controller of each County the RDAs' former responsibility to calculate and allocate the AB 1290 payments to affected taxing entities. The costs imposed by the Bill would be funded by fees paid by RDAs to the Auditor-Controller.

SB 360 raises a critical concern for the Auditor-Controller regarding our County's potential liability exposure for failure to make the RDAs' payments accurately. The task, as the SCO's report repeatedly points out, is extremely complex. County Counsel and the Auditor-Controller are working with the Senate Local Government Committee consultant to add language to SB 360 that limits the time in which allocations could be

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challenged to within 90 days of the last annual payment; otherwise, the Auditor-Controller's allocation is deemed correct. Coincidentally, the Auditor-Controller recently restructured their tax allocation data processing system and it is designed to meet the needs of the proposed process.

If you have any questions regarding this matter, please contact me or Ms. Watanabe, or your staff may contact Lari Sheehan at (213) 893-2477, or Susan J. Linschoten at (213) 974-8361.

WTF:WLW
SJL:os

c: Executive Officer, Board of Supervisors
County Counsel